

DEPARTMENT OF STATE REVENUE
LETTER OF FINDINGS: 98-0577
Indiana Adjusted Gross Income Tax
For 1995

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ISSUE

I. Net Operating Losses – Adjusted Gross Income Tax.

Authority: IC 6-3-2-2.6; IC 6-8.1-5-1(b); 45 IAC 3.1-1-6; I.R.C. § 172(b)(1)(A)(ii); I.R.C. § 172(b)(3); I.R.C. § 172(c), (d); Treas. Reg. § 1.172-2; Treas. Reg. § 1.172-3.

Taxpayer argues that it was entitled to carry forward a net operating loss and that – as a result – taxpayer did not owe Indiana adjusted gross income tax for 1995.

STATEMENT OF FACTS

The Department of Revenue (Department) determined that taxpayer owed a delinquent state income tax liability for 1995, offset a year 2000 refund otherwise owed taxpayer, and sent taxpayer a notice to that effect. Taxpayer challenged the decision. Taxpayer did so on the ground that a net operating loss – carried forward from 1987 – more than compensated for any 1995 tax liability.

Taxpayer and the Department exchanged correspondence without resolving the matter. The unresolved issue was treated as a protest. Because taxpayer's representative declined the opportunity to take part in an administrative hearing, this Letter of Findings was written based upon the information contained within the Department's file and the correspondence furnished by taxpayer's representative.

DISCUSSION

I. Net Operating Losses – Adjusted Gross Income Tax.

According to taxpayer, her farm business incurred a net operating loss of approximately \$200,000 in 1987. Taxpayer then carried forward the 1987 loss to 1988 entirely offsetting taxpayer's income received during that year. Taxpayer carried forward the "unused" portion of the loss to 1989 thereby offsetting the 1989 income. Because the original loss was substantial and the personal income received during each following year was comparatively small, the original net operating loss was carried forward again and again offsetting each subsequent year's income. Taxpayer repeated this process through 1995 after which nothing remained of the original \$200,000 loss.

The Department's only challenge was to taxpayer's 1995 calculation. The Department requested documentation substantiating the source and nature of the 1987 loss. Taxpayer's representative supplied copies of the underlying federal return and copies of the taxpayer's state returns. The Department remained unsatisfied with the documentation supplied and the explanations offered.

Taxpayer's contention is that the 1987 net operating loss offset any potential 1995 tax liability. The rule governing net operating losses for individuals is found at 45 IAC 3.1-1-6 which states in part as follows:

The following provisions pertain to the use of a Federal net operating loss deduction as it applies to an individual subject to the Indiana Adjusted Gross Income Tax Act. The amount of the net operating loss that may be carried back and forward for Indiana income tax purposes shall be that portion of the Federal net operating loss allocated to Indiana for the taxable year the operating loss is sustained.

Indiana treatment of individual net operating losses is governed by the provisions of the federal law concerning corporate net operating losses. IC 6-3-2-2.6. I.R.C. § 172(c), (d), defines a net operating loss as the excess in allowable deductions over gross income computed under the law in effect during the loss year. Treas. Reg. §§ 1.172-2; 1.172-3. This net operating loss (NOL) can be carried back and used as a deduction for the two years preceding the loss year. If some of the NOL has not been used up by the carryback, it is carried forward into the 20 years after the loss year and used as a deduction. I.R.C. § 172(b)(1)(A)(ii). Alternatively, taxpayer may elect to forgo the entire carryback period. I.R.C. § 172(b)(3). If this election is made, the loss will then be carried forward only.

Taxpayer has the responsibility to show that the 1995 income was offset by the serial carry forward of the 1987 NOL. IC 6-8.1-5-1(b) states that, "The notice of proposed assessment is prima facie evidence that the department's claim for the unpaid tax is valid. The burden of proving that the proposed assessment is wrong rests with the person against whom the proposed assessment is made."

The Department has no quarrel with taxpayer's calculations because the serial carry forward calculations appear to be correct. However, what is missing is any sort of explanation as to the manner in which the \$200,000 was originally incurred or how that loss was calculated. The Department is left to speculate as to the nature and source of this loss. (What did taxpayer lose? How did taxpayer figure that it was worth \$200,000?) The Department has no reason to doubt taxpayer's veracity or good intentions, but with nothing more to go on than taxpayer's repeated assurance that there *was* a \$200,000 loss in 1987, the Department is unable to conclude that taxpayer has met her burden of demonstrating that the proposed assessment is incorrect.

FINDING

Taxpayer's protest is respectfully denied.